UNITED STATES DEPARTMENT OF AGRICULTURE

AGRICULTURAL ADJUSTMENT ADMINISTRATION

Administered Price and Market Price

Highlights: In a free market, supply and demand determine price.

In an administered market, price and demand determine supply.

A market price is one which is made in the market as the result of the interaction of buyers and sellers. The prices of wheat and cotton are market prices, as are the prices of many other farm products.

An administered price is essentially different. It is a price that is set by administrative action and held constant for a period of time. A company maintains a posted price at which it will make sales. Or it simply has its own prices at which buyers may purchase or not as they wish. These are administered prices. Many wholesale and most retail prices are administered rather than market prices.

Thus, prevailing devices for price making work one way for the seller of manufactured and processed goods, and transportation and utility services, and another way for the seller of farm products.

In 1931 the 200 largest manufacturing corporations in the country controlled more than 55 percent of all manufacturing assets.

In 1935 it has become evident that, from the standpoint of both agriculture and industry, the great need is a direct effort at increased industrial output—an industrial adjustment to balance agricultural adjustment.

I. Operation of Double Market

Farmers often say that they are obliged to buy in one market and sell in another. The market in which they buy, they observe, maintains comparatively rigid and inflexible prices. On the other hand, the market in which they sell is extremely sensitive to the influences of supply and demand conditions.

On account of this apparent dual market set-up farmers find that for the commodities they buy they must pay a price which tends to vary but little as conditions change. Price for things bought by farmers does not decline in a falling market in anything like the proportion by which price for things they sell falls.

Effect of Law of Supply and Demand.—When farmers complained of the disadvantage worked upon them by this functioning of what appears to be two separate markets, they have been told that the economic law of supply and demand makes it necessary.

But it is a law that works one way for the seller of manufactured and processed goods, and transportation and utility services, and another way for the seller of farm products.

Farmers are law-abiding, but for a long time they have been outspoken in their resentment of the way this assumed economic law

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acts. They have repeatedly challenged its principle, which their experience and their common sense have convinced them is wrong.

They know, of course, that the law of supply and demand applies with unfailing regularity in setting the price for commodities which they send to the market.

How the Market Works With Hogs and Wagons.—Take hogs, for example—it could be any other farm product. Let us say a farmer sends animals to market in the early morning of a given day. The price that he gets for his hogs depends upon market conditions—how many other farmers have sent in hogs and how many people are there to buy. The prices are the result of a bargain struck under these conditions. When the farmer sends his hogs, he does not know how much he is going to get for them. He is sure that they will be sold, because he is not going to pay the freight to have them shipped back to him. But he cannot tell what the price will be.

Contrast the fate of a wagon with the fate of a hog. In the offices of a wagon manufacturer the managers decide upon the price for their product. They print their price lists and mail them out to salesmen. They may arrange ahead of time to buy the materials which go into the wagon, at prices which promise to give them a profit on each wagon at the price which they decide upon for it. They do not know how many wagons they are going to sell. But they do know at what price they will be sold.

How Double Market Works.—The extent to which farm prices are governed by open-market conditions as contrasted with the administered price of a double wagon is well illustrated by the variations in the following table showing the number of hogs, bushels of corn, pounds of cotton, and bushels of wheat needed to buy a double wagon in the years from 1921 to 1934:

Number of bales of cotton (500 pounds), bushels of wheat, bushels of corn, and 200-pound hogs needed to buy a standard 2-horse farm wagon in the United States, 1921–34

Year	Average wholesale price of double wagon	Number bales of cotton needed to buy double wagon	Number bushels of wheat needed to buy double wagon	Number bushels of corn needed to buy double wagon	Number 200-pound hogs needed to buy double wagon
1921	$118. 27	2. 07	106	212	7. 6
1922	100. 80	. 97	104	170	6. 0
1923	111. 05	. 79	117	140	7. 8
1924	111. 15	. 93	97	121	7. 5
1925	96. 90	. 93	66	99	4. 5
1926	103. 07	1. 54	80	148	4. 4
1927	103. 07	1. 15	86	133	5. 4
1928	103. 07	1. 14	97	119	6. 1
1929	94. 24	1. 08	90	109	5. 0
1930	93. 83	1. 81	125	122	5. 3
1931	86. 60	2. 83	203	176	7. 4
1932	79. 19	2. 61	210	287	11. 5
1933	78. 97	1. 82	121	220	11. 2
1934	81. 31	1. 32	99	131	9. 7

Crop Reporting Board, Bureau of Agricultural Economics.

What Causes the Contrast in Price?—The contrast between the price of the farmer's hog and the price of a wagon is the contrast between two kinds of price determination.

There are two kinds of markets. Economists call one a "free market." They call the other an "administered market." (See charts on pp. 6 and 7.)

The operation of a free market was clearly shown in the case of most farm products before the Agricultural Adjustment Act was passed. The individual farmer produced wheat or not, depending upon what he expected the price of wheat to be, and he offered the grain for what it would bring in the market.

He had no real control over either the total amount of wheat produced or the market price of wheat. His contribution to the total supply was too small to give him any control over the industry in which he, an individual wheat producer, usually had but a very modest share.

While farmers, as small units in the great business life of the Nation, were selling in a free market, industrial corporations—factories, mills, public utilities, railroads, and other corporate enterprises—were enjoying advantages in an entirely different kind of market, an "administered market."

II. How Supply, Demand, and Price Act in Market

There is plenty of proof that there has been a basic change in the manner and the force with which demand, supply, and price come together and adjust themselves in the market of today. No longer does the market operate in the same way for all who buy and sell therein. By means of managed price-fixing, relatively unknown a few years back, markets can be set up to favor those who can exercise control.

In 1776 Adam Smith set forth in his "Wealth of Nations" the law of supply and demand. That law applied to conditions as Smith found them in his lifetime. Then people did business largely as individuals. The units of business in his economy were like atoms. The units were composed of workers who employed their own tools, one-man businesses, or business organizations so small that for most purposes they could be considered as one-man affairs.

Organization of Industry in Large Units.—Up to 1933 most of agriculture still belonged in the Adam Smith picture.

But the unit organization of factories, mills, public utilities, railroads, and other corporate enterprises had significantly altered. Today a large part of industrial activity has been concentrated into large units. Individual men who control the business policy of these large unit organizations can and do make production conform to price. They dictate industrial policy.

Hence the type of price arrived at in the market in which they trade is one which represents the balancing of production and demand at a price. That is to say, they first decide upon the price at which they will sell their product or service. Price thus becomes an arbiter, not a result, as it is in the functioning of the law of supply and demand in a free market.

What Is Difference Between "Free" and "Administered" Markets?—In a free market, supply and demand determine price. In an administered market, price and demand determine supply.

This is how the administered market works to the advantage of businesses which can employ it. The consuming public has certain unsatisfied wants for industrial goods and services—wagons, farm machinery, aluminum products, telephone, telegraph, and transportation services, and a large number of other wants. These unsatisfied wants stand for demand. Up to the point at which the consuming public absorbs products at administered price, and no further, industry permits supply to reach the market.

How is industry able to control industrial policy? Not solely through monopoly, as is frequently asserted. It may happen due to the fact that control becomes inherent in the relatively small number of units of production which bid for business in modern industrial society.

Two hundred corporations controlled about 54 percent of all non-financial wealth in this country in 1931. In manufacturing alone a very high degree of concentration exists. Consideration of manufacturing excludes the highly concentrated fields of railroads and public utilities. Neither does it take into account the relatively unconcentrated construction and distribution industries.

In 1931 the 200 largest manufacturing corporations in the country controlled more than 55 percent of all manufacturing assets. Contrast this condition with the small-scale business of Adam Smith's day, and it is evident that the law of supply and demand as stated in his historic work is not adapted to conditions today.

What Is Difference Between "Free" and "Administered" Prices?—The difference between market prices and administered prices is clear.

A market price is one which is made in the market as the result of the interaction of buyers and sellers. The prices of wheat and cotton are market prices, as are the prices of many other farm products.

An administered price is essentially different. It is a price that is set by administrative action and held constant for a period of time. A company maintains a posted price at which it will make sales. Or it simply has its own prices at which buyers may purchase or not as they wish. These are administered prices. Many wholesale and most retail prices are administered rather than market prices.

Economic Rules of Earlier Period Outgrown.—Adam Smith knew, as accurate and alert observers know today, that there can be no wealth of nations in an economy based upon rules which no longer can be made to work. The liberal doctrines which he advanced discredited the economic policy of the period before he wrote.

Today, certain of the rules of economic behavior which he then advanced as something new have in turn been superseded. They are as out-of-date as are the tools which Smith's neighbors used in harvesting and threshing their grain.

What Caused Collapse of Agriculture in 1921?—The collapse of American agriculture in 1921, and of American industry after 1929, was due in large part to the fact that some prices, made in the market, had collapsed, while other prices, administered by individuals

or corporations, had been held relatively rigid. Recovery of both agriculture and industry required that this fact be recognized and that something be done about it.

III. Farmers Adopt New Policy

Farmers have followed a new pattern in taking steps to throw off the handicap they meet when they sell in one market and buy in another. Through production-control programs and other measures designed to govern supply, they have been able to free themselves, with respect to certain commodities, from some of the disadvantage of selling in what was mistakenly known as a " free market." Agricultural adjustment has given them a means through which collectively, they have some power of administration over the market in which they sell their own products.

Therefore, the prices for farm commodities to which they have been able to apply adjustment measures are, to a limited extent, under control. By making the supply of those commodities conform to the result of demand and price in some cases farmers have been able even to maintain relatively fixed prices.

But in agriculture, as in manufacturing, there is a definite limit to possible improvement through the device of making administered prices upon commodities.

Need for Industrial Adjustment.—In 1935 it has become evident that, from the standpoint of both agriculture and industry, the great need is a direct effort at increased industrial output—an industrial adjustment to balance agricultural adjustment.

An increase in industrial output would be attended by the reemployment of industrial labor that was laid off during the depression. The reemployment of industrial labor would result in increasing the buying power of city workers. Thus a greater demand for farm products would be created.

Increased industrial activity is basic to a restoration of the farmer's former standard of living. It is the real way to reemployment and greater incomes for city workers. And it is the most important single factor in restoring profits to industry.

A new wealth of nations calls for a restoration of balance between industrial and agricultural production.

Agriculture Cannot Further Cut Production Without Injury.—Agriculture has done as much as it can toward restoring this balance. It cannot further restrict production without doing injury to itself and to the consuming public.

Farmers will have to continue to control their production if they wish to prevent another collapse in the price of agricultural commodities. But industry can do a great deal in the interest of restoring the required balance. It can greatly increase production and in so doing benefit invested capital, labor, the consuming public, and farmers.

A few comparative figures clearly indicate how the predepression balance between industry and agriculture was changed by industry's policy of drastic reduction of production between 1929 and 1934.

Industry's " Plow-Up " of Production Greater Than That of Agriculture.—Factory production in industries using nonagricul-

tural raw materials in 1934 had decreased 42 percent from the 1929 level. For the same period the volume of factory production using agricultural raw materials was down only 15 percent. Industry's "plow-up" of production during the period was 27 percent greater than agriculture's. (See charts, pp. 6 and 7.)

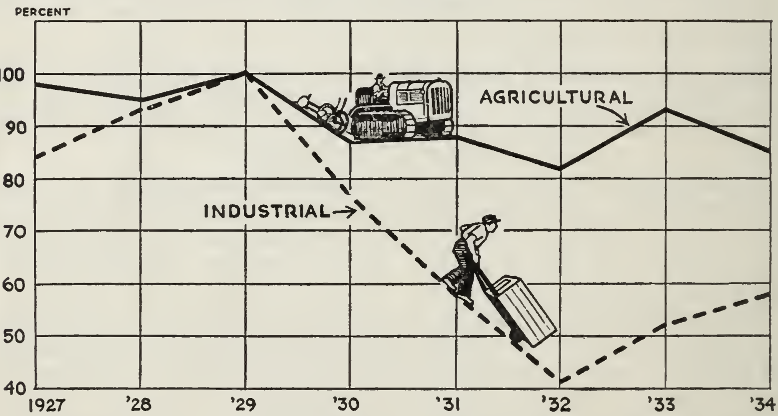
The price situation was just the reverse. Farm-product prices in 1934 were 39 percent lower than 1929. Industrial prices were only 14 percent lower.

Industrialists, making use of an administered market, cut supply deeply, while price remained comparatively rigid.

Agriculture, trading in a free market before 1933 but provided with some of the advantages of an administered market after that year, cut supply only a small amount and took a sharp decline in price.

The production of industrial goods in 1934, in relation to the production of farm products, was about 35 percent less. This fact naturally shows up in an exchange value of farm products for industrial products in 1934—30 percent lower than in 1929.

PRODUCTION KEPT UP BY AGRICULTURE



While agriculture continued to produce at a high level, industry curtailed its output. The volume of agricultural products processed in domestic factories remained on a level approximately 15 percent below the 1929 level throughout the depression, but industrial production declined nearly 60 percent below the 1929 level in 1932, and during 1934 averaged more than 40 percent below.

In general, farm production programs aim at production maintained for domestic needs. The programs have no drastically limited supplies. If farmers had reduced production more nearly to the extent that the volume of industrial production and domestic purchasing power was lowered, they might have attained higher prices and greater returns.

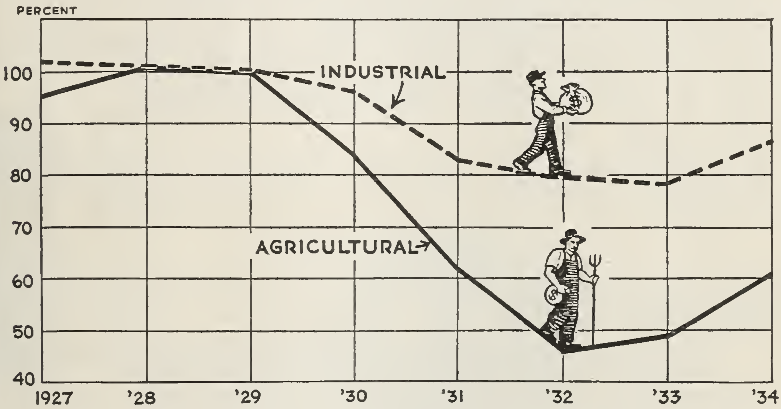
Farmers have refrained from a policy which would harm the Nation even though it brought agriculture increased returns. Agricultural production has stopped short of such a policy in seeking to restore balance as among the several branches of agriculture and to restrain production of export crops until foreign markets can be regained. To the extent that these measures have resulted in improving the purchasing power of farm products and of increasing

farm income the objectives of the farm program have been approached. The full restoration of predepression balance as between agriculture and industry depends upon future industrial policy.

IV. Next Step Is Increased Industrial Production

The logical next step in the correction of past mistakes in the Nation's productive system is for industry to increase volume of production and to decrease the price of industrial products. That the general interests of the country would be best served if industry adopted a flexible price policy—more production, lower prices—is indicated by the experience of recovery from former business depressions. Increased industrial volume at lower industrial prices has in the past proved effective in restoring general prosperity. The advantages of a flexible price policy for industry are also evident in the long-time relationships between agricultural and industrial prices.

PRICE KEPT UP BY INDUSTRY



The disparity between industrial and agricultural prices is shown above. Agriculture sold in a free market. Industrial prices in 1934 averaged approximately 15 percent below the 1929 level, but agricultural prices which, in 1932, averaged about 55 percent below the 1929 level, were still nearly 40 percent below the 1929 level during 1934.

Buying Power of Farm Products Gains As Industry Expands.—The United States is becoming more and more industrialized. It has both industrial- and farm-production capacity far beyond its present demand. Industrial production under such circumstances expands much more rapidly than agricultural production because demand for agricultural products is closely related to population growth. It is natural, therefore, for prices of agricultural products to gain in relative purchasing power. This was the long-time trend in the United States for more than a century. This trend must be restored if industrial activity is to regain its 1929 level and agriculture is to regain its predepression balance in the national production system.

Industrial Efficiency Increased.—By means of control systems industry has made possible remarkable increases in the efficiency of industrial production within single enterprises. The large number of

workers brought into a single organization has allowed a high degree of subdivision of labor and the use of complicated series of machines so that the volume of production has been expanded far beyond the capacity of the same number of workers operating independently.

Organization has made for rapid and extensive development of new methods. The more efficient system in turn has increased the advantages of administrative control. The possibility of a high standard of living for all rests on these two dependent factors.

Concentration of economic activity brought increased productivity. It also destroyed the free market and disrupted the operations of the law of supply and demand in a great many industries and for the business structure as a whole.

The Nation's problem today is that of holding the advantages that concentration of industry has created, and at the same time making the new system evolved by it work out for the general welfare.

Full Recovery Depends on Balanced Industrial Production.— The Agricultural Adjustment Act provided farmers with a means of attaining some of the advantages of concentration that industry, by means of practical management, enjoys. It is possible that eventually they may not be obliged to buy in the protected domestic market and sell in the open world market. They have the means of reaching a plane of economic equality with industrial producers.

Farmers have approached a balance of their production to the Nation's needs.

Not until industry has succeeded in balancing its production by creating greater abundance will recovery be fully realized.

Suggested References

Copies of the following publications may be obtained from the sources noted as long as supplies are available:

The Need for an Industrial Production Program as a Basis for Sound Price and Employment Policies, by Louis H. Bean. Office of Information, United States Department of Agriculture, Washington, D. C. (Free.)

The Need for a Flexible Industrial Price Policy, by Louis H. Bean. Office of Information, United States Department of Agriculture, Washington, D. C. (Free.)

Industrial Prices and Their Relative Inflexibility, Senate Document No. 13, Superintendent of Documents, United States Government Printing Office, Washington, D. C. (5 cents, no postage stamps.)

Facing the Facts in the Agricultural Situation, G–42; Correspondence, Records, and Printing Section, Division of Information, Agricultural Adjustment Administration, Washington, D. C. (Free.)

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